



OFFICE OF MANAGEMENT AND BUDGET

Isiah Leggett
County Executive

Joseph F. Beach
Director

MEMORANDUM

March 27, 2009

TO: Interested Readers

FROM: Joseph F. Beach, Director

SUBJECT: FY10-15 Fiscal Plan

Executive Summary:

The County Executive's highest priority during the budget process this year was to produce a fiscally prudent and sustainable budget that preserves public safety services, education, and the County's safety net for its most vulnerable residents. The Executive also made an early commitment to propose a budget with property taxes at the Charter limit.¹ The challenge was to meet these requirements and close an unprecedented projected gap of nearly \$590 million.

This challenge was met. The Executive recommends a \$690 credit for each owner-occupied residence which keeps property taxes at the Charter limit and supports a progressive property tax structure in the County. The Executive's recommended budget increases overall spending by just 1.9 percent, the lowest increase in 18 years. Tax supported spending across all agencies increases only 1.1 percent, while the County government tax supported budget actually decreases 0.4 percent compared to FY09. This follows increases of 6.9 percent and 1.6 percent respectively in the Executive's first two recommended tax supported budgets for the County government. Continuation of this pullback in spending is necessary to correct the structural imbalance in the operating budget by bringing current and expected expenditures into alignment with revenues.

While this budget repositions Montgomery County for the future, it is unlikely these measures to restrain spending are complete with the FY10 operating budget. Given the severity of the current recession and declining revenues, FY11 and perhaps ensuing fiscal years will require continued restructuring of County expenditures, especially personnel costs which comprise 80 percent of County costs. Significant fiscal pressures remaining on the horizon include rising employee compensation and benefit costs, continued funding of retiree health insurance expenses, increased demand for new and expanded services or restoration of service reductions, the impact on the operating budget from capital investment, and continued economic deterioration. This challenge is evident in the current projected

¹ Section 305 of the County Charter limits the growth in real property tax revenues in a fiscal year to the rate of inflation, excluding new construction, development districts, and other minor exceptions. The Council may override this limitation with an affirmative vote of nine Councilmembers.

FY11 budget gap of more than \$370 million, not including potential additional reductions in Federal and State Aid, further complicating the County's ability to plan for the FY10-15 period.

Background:

The recommended FY10-15 Fiscal Plans for the tax supported and non-tax supported funds of the agencies of County government are provided for your information. Portions of this material were initially published in the FY10-15 Recommended Operating Budget and Public Services Program (March 16, 2009).² As in past years, this information is intended to assist the County Council and other interested parties review the County Executive's recommended budget during the Council's budget worksessions this spring.

Interested readers should note that the fiscal plans included in this publication are not intended to be prescriptive, but are instead intended to present one possible outcome of policy choices regarding taxes, user fees, and spending decisions. Other important assumptions are explained in footnotes at the bottom of each fiscal plan display. One significant benefit of presenting multi-year projections is that the potential future year impacts of current policy decisions can be considered by decision makers when making fiscal decisions in the near term. The Executive's fiscal policies support:

- prudent and sustainable fiscal management: constraining expenditure growth to expected resources;
- identifying and implementing productivity improvements;
- avoiding the programming of one-time revenues to on-going expenditures;
- growing the local economy and tax base;
- obtaining a fair share of State and Federal Aid;
- maintaining prudent reserve levels;
- minimizing the tax burden on residents; and
- managing indebtedness and debt service very carefully. Once again, all of the major rating agencies have recognized these policies by continuing to affirm our coveted AAA credit rating, the highest possible.

Because of the unusually severe decline in projected revenues since approval of the FY09 budget last May, it was necessary for the County Executive to recommend certain measures for FY10 that he had strongly resisted in the past. He is recommending a temporary reduction in tax supported reserves from 6 percent of resources to 5 percent, which released \$39 million to the operating budget. In addition, the Executive reduced PAYGO³ by nearly \$29 million and deferred the \$26 million increase for retiree health insurance pre-funding. These measures were necessary to balance the FY10 budget and sustain existing critical services. The Executive recommends replacement of these resources to their policy levels as quickly as possible.

Finally, the Executive recommends releasing the designated reserves for the Interagency Technology Fund, Fibernet, and Landlord Tenant Affairs/Common Ownership Communities. In the past,

² In addition to these two documents, the reader is encouraged to review other County fiscal materials such as the Comprehensive Annual Financial Report for the year ended June 30, 2008; the Annual Information Statement published by the Department of Finance on January 15, 2009; and Economic Indicators data. Budget and financial information for Montgomery County can also be accessed on the web at www.montgomerycountymd.gov.

³ Current revenue that is substituted for debt in capital projects that are debt eligible or used in projects that are not debt eligible or qualified for tax-exempt financing is referred to as PAYGO, or "pay as you go" funding. The County's policy is to program at least 10 percent of planned General Obligation bond issues as PAYGO in the capital budget.

these designations were included as part of the County's 6 percent reserve policy, which has caused some confusion about the availability of these funds and their impact on the County's overall reserves.

Releasing the designations does not reduce in any way the amount of funds for these programs, but simply clarifies the presentation of the County's reserves and makes obvious that any use of these funds would be a draw on the County's resources.

Fiscal Plan for the Tax Supported Funds:

The recommended fiscal planning objectives for FY10-15 for the tax supported funds are:

- Adhere to sound fiscal policies.
- Maintain property taxes at the Charter limit by providing a \$690 credit to each owner-occupied household.
- Assume property tax revenues at the Charter Limit during FY11-15 in the fiscal plan.
- Temporarily reduce total tax supported reserves (operating margin and the Revenue Stabilization Fund) from 6 percent of total resources to 5 percent of total resources. Reserves are restored to 6 percent in FY11-15 of the fiscal plan.
- Manage fund balances in the non-tax supported funds to established policy levels where applicable.
- Assume current State aid formulas, but continue successful strategies to increase State (and Federal) operating and capital funding.
- Maintain priority to economic development and tax base growth:
 - Seize opportunities to recruit and retain significant employers compatible with the County's priorities;
 - Give priority to capital investment that supports economic development/tax base growth.
- Maintain essential services.
- Limit exposure in future years to rising costs by controlling baseline costs and allocating one-time revenues to one-time expenditures, whenever possible.
- Manage all debt service commitments very carefully, consistent with standards used by the County to maintain high credit ratings and future budget flexibility. Recognize the fixed commitment inherent in all forms of multi-year financing (long-term bonds, shorter-term borrowing, and lease-backed revenue bonds) that must be accommodated within limited debt capacity.
- For capital investment, allocate debt, current revenue, and other resources made available by the fiscal objectives above according to priorities established by policy and program agendas.
- Program PAYGO at least 10 percent of anticipated General Obligation Bond levels to contain future borrowing costs in FY11-15.
- For services, allocate resources consistent with policy and program agendas.

The major challenges for FY10-15 will be to contain on-going costs, preserve essential services, make improvements in other services including education, public safety, affordable housing, transportation, and health and human services, as the housing market and general economy continue to show signs of persistent weakness.

Fiscal Plans for the Non-Tax Supported Funds:

By definition, each of the non-tax supported (fee-supported) funds is independent, covering all operating and capital investment expenses from its designated revenue sources. The fiscal health of each fund is satisfactory, though looking ahead some funds will need to meet expected challenges by rate adjustments and/or expenditure management decisions. One continuing challenge for some of these funds

relates to the impact of pre-funding retiree health insurance costs. The County Executive recommends modifying the fund balance policy of the Water Quality Protection Fund. A revised fund balance policy will be transmitted to the County Council under separate cover.

Conclusion:

Montgomery County's fiscal health is strong as a result of its underlying economy and the financial management policies endorsed by its elected officials. Nonetheless, the County continues to face significant challenges in the years ahead. The FY10-15 Fiscal Plans reflect these challenges in their assumptions and projections.

Comments on the Fiscal Plans that follow are encouraged as opportunities for improvement. Office of Management and Budget and Finance staffs of the County government, and Finance staff of the other agencies, are available to assist in the Council's deliberations.

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Attachment: FY10-15 Fiscal Plan for Montgomery County, Maryland

c: Isiah Leggett, County Executive
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